Transgrid

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Attachment 6: Rules pre-conditions

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1. Purpose and key messages

This Attachment forms part of Transgrid's application to reopen the 2023-2028 Revenue Determination in accordance with clause 6A.7.1 of the NER (**Application**).

As outlined in section 1.4 of the Main Application, the Contract Failure and its implications satisfy each of the preconditions in clauses 6A.7.1(a) and (b) of the National Electricity Rules (**NER**). This Attachment outlines the event comprising a Contract Failure and provides further details on each precondition and explains how the requirements have been met.

Key messages

- **Event:** The event, the subject of this Application, is that due to the accumulation of circumstances that had adversely impacted PEC and based on information and analysis obtained between August and October 2023, Transgrid recognised and accepted that the construction of PEC would not be completed by Secure Energy Joint Venture (**SEJV**) under the existing Engineering, Procurement and Construction (**EPC**) contract and, if PEC were to proceed, an alternative arrangement to delivery under the EPC contract would be necessary. See section 2 below for the complete definition.

- **'Contract Failure':** the event necessarily involves some complexity given the circumstances and scale of the project and the issues that arose. It is clear from the NER that clause 6A.7.1 can encompass a multi-faceted event as it refers to an event including "a series of events or a state of affairs". For the convenience of readers, Transgrid has given this event a short-hand description of 'Contract Failure'. However, this term is a label – it is not reference to an industry or legal concept.

- **Reasonable control:** the Contract Failure occurred as a result of an accumulation of circumstances beyond Transgrid's reasonable control. The EPC contract was appropriate and sound when entered into and Transgrid managed PEC in accordance with the terms of that contract.

- **Reasonable foreseeability:** the Contract Failure (or an event of a similar kind) could not have been reasonably foreseen by Transgrid at the time of making the revenue determination. Transgrid reasonably believed that the issues experienced by the project could be managed within the terms of the EPC contract, including the substantial performance guarantees and security provided by Elecnor Australia's parent company.

- **Interpretation of reasonable foreseeability:** the date to assess reasonable foreseeability is 2 December 2022, being the date that Transgrid submitted its revised revenue proposal for the 2023-2028 regulatory control period. The standard of foreseeability to be applied should be considered in the context of the mechanism for determining a TNSP's capex allowance through the revenue determination process in Chapter 6A of the NER.

- **Reliability and security:** a failure to rectify the adverse consequences of the Contract Failure would have likely materially adversely affected the reliability and security of the relevant transmission system. The material adverse impacts include compromised Electricity Statement

of Opportunities (**ESOO**) reliability, growth of the unserved energy gap in South Australia, reduced New South Wales transfer capacity and compromised system security.

2. Occurrence of an event within the 2023-2028 regulatory control period

Clause 6A.7.1(a)(1) of the NER requires the occurrence of an event in the 2023-2028 Regulatory Control Period (**RCP**) which is beyond the reasonable control of the TNSP, and which could not reasonably have been foreseen by the TNSP at the time of the making of the revenue determination for the 2023-2028 RCP.

2.1 The Event

2.1.1 Event definition

The event, subject of this Application, is a Contract Failure. The Contract Failure is that:

- as the result of the accumulation of circumstances that had adversely impacted the contractor's ability to deliver PEC, and
- based on information and analysis obtained by Transgrid between August and October 2023, which revealed that Elecnor Australia was in a precarious financial position and faced significant financial losses under the terms of the EPC contract,

Transgrid's Board recognised and accepted on 25 October 2023 that the construction of PEC would not be completed by SEJV under the existing EPC contract and, if PEC were to proceed, an alternative arrangement to delivery under the EPC contract would be necessary.

Transgrid has identified this date as the date of the Contract Failure as on this date key analysis and conclusions were presented to and accepted by the Transgrid Board. It was at this Board meeting that Transgrid management first recommended to the Board that Transgrid had to substantially depart from the existing terms of the EPC contract to deliver PEC which recommendation was recognised and accepted at that Board meeting.

A summary of the analysis and conclusions are detailed in section 9 of Attachment 2.

Circumstances and new information underpinning the event

The accumulation of circumstances adversely impacting the contractor's ability to deliver PEC are described in section 2.2 of the Main Application and sections 6 and 7 of Attachment 2 and included:

- inflation of materials and labour
- skilled labour shortages, delayed visa approvals and concentration of infrastructure and energy projects in Australia
- the Clough voluntary administration which impacted project management systems and required the transfer of labour agreements, and
- major New South Wales severe flooding events.

The information and analysis that Transgrid obtained between August and October 2023 which revealed Elecnor Australia's precarious financial position included:

- obtaining open book access to the project accounts (noting that Transgrid did not have a contractual right to such access under the EPC contract)
- Transgrid developing its own Integrated Master Schedule (**IMS**) to identify a realistic programme which showed material delays beyond those forecast by Elecnor Australia with delay increasing the costs to complete PEC due to the challenging cost environment

- based on the IMS, Transgrid preparing its own detailed forecast cost to complete based on the actual underlying costs disclosed by Elecnor Australia which showed a forecast cost to complete which was substantially greater than that previously forecast by Elecnor Australia
- commissioning Fission to provide an independent view of the forecast cost to complete
- in light of the costs involved, reviewing the steps to enforce the parent company guarantee and recognising the substantial challenges in doing so
- systemic delays in payments to the suppliers and subcontractors
- cash constraints alleged by Elecnor Australia, in addition to project cashflow showing that the project would become cashflow negative on a cumulative basis in November 2023, and
- the emerging cashflow issues and the forecast costs to complete exposing Elecnor Australia to risk of insolvency in the absence of support.

Further project cashflow information and an external analysis on the risk of insolvency became available to Transgrid during November and December 2023 that confirmed the likely insolvency of Elecnor Australia in the absence of support.

Consistency with clause 6A.7.1(a)(1) of the NER

The term 'Contract Failure' is not a reference to a concept at law or other regulatory or industry precedent. It is a label that Transgrid has given to the event to assist readers when considering this Application and it comprises the accumulation of interrelated circumstances occurring over a period culminating in a recognition that the project would not be completed absent a new delivery arrangement.

Transgrid recognises the event is not a simple, singular incident and involves both exogenous circumstances (the underlying circumstances and the obtaining of information) and an endogenous circumstance (being Transgrid Board's recognition and acceptance of the effects of those circumstances). Even so, this event is consistent with clause 6A.7.1(a)(1) of the NER:

- As described in section 1.5 of the Main Application, 'event' is intended to be a broad concept that accommodates a variety of circumstances which is appropriate given that the reopener provisions are intended to respond to a wide variety of occurrences including a series of events or a state of affairs. This is in contrast to pass-through events under clause 6A.7.3 of the NER which are narrowly defined, but have a much lower monetary threshold. For the reopener provisions, the scope of eligible reopener events is limited by the pre-conditions discussed below.
- The Contract Failure that has occurred is of the kind to which the reopener provisions should apply.
- The Contract Failure is primarily based on exogenous circumstances. Transgrid recognises there may be concern that the event includes the Board's recognition of the Contract Failure being the point at which rectification commenced. However, it is necessary to consider the event with realistic regard to the regulatory, commercial and contractual context in which Transgrid was operating. The review of such exogenous circumstances, the impact of these circumstances on the viability of the project and any subsequent decisions about major capital expenditure must intrinsically involve proper governance and decision making by Transgrid.
- The inclusion of an endogenous element, relating to Board decision making, does not mean the event is within Transgrid's reasonable control. Rather, the Board's recognition that an alternative delivery arrangement was required, and Transgrid's subsequent commitment of additional capex, in order to

ensure completion of the project, were prompted by the succession of external challenges that confronted the project. The Board responded to those exogenous circumstances so as to achieve completion of the project in a way that would maximise the net benefit to consumers. Taken together, the broad concept of an 'event' and the requirement that the event must not be within a TNSP's *reasonable* control allows the AER to evaluate an event that comprises both exogenous circumstances and a TNSP's reasonable response to those circumstances. Clause 6A.7.1(a)(1) imposes no requirement that the event must be "exogenous", or *wholly* outside a TNSP's control.

- For example, if Transgrid were required to posit a purely exogenous event, it might be said that Transgrid was required to enforce its rights under the EPC contract to the point of Elecnor Australia also falling into insolvency, before Transgrid then proceed to tender for and engage a new contractor under different contract terms. But even that scenario would include an endogenous element – namely, the Transgrid Board electing not to take steps to pursue other modifications to the original contract arrangements that might avoid insolvency of the remaining joint venture party.
- Indeed, this was a choice that the Transgrid Board faced and considered. As described in 2.3 of the Main Application, one of the options available was to take no steps to rectify the Contract Failure, other than to enforce Transgrid's existing contractual rights to the point of Elecnor Australia also becoming insolvent. However, this was not the best option for consumers. It would be a perverse outcome, and contrary to the National Electricity Objective, if an overly narrow interpretation of an event under clause 6A.7.1 were to require a sub-optimal option to be taken to be able to access the reopener mechanism.

Moreover, if an event could not include any element of commercial decision-making by a TNSP, then it would follow that a TNSP would be unable to make any increased capex commitments in response to a major unforeseen and adverse effect without first obtaining AER approval for a capex reopener. The risks that would create to consumers' interests and to timely build-out of the Integrated System Plan (**ISP**) optimal transmission pathway are so obvious as to need no further explanation. The Contract Failure occurred on 25 October 2023, after the making of the 2023-2028 Revenue Determination and within the current 2023-2028 RCP.

2.2 Event beyond Transgrid's reasonable control

In evaluating whether the event was beyond Transgrid's reasonable control, the AER must have realistic regard to the contractual, commercial and regulatory context in which Transgrid was operating. Transgrid considers that the Contract Failure was beyond its reasonable control for the following reasons.

First, for the reasons set out in section 4.1 of Attachment 2, although the EPC contract limited Transgrid's ability to engage in direct day-to-day management of the project, that contract framework was sound and appropriate when it was entered into:

- The EPC contract was procured via a comprehensive and competitive procurement process. The procurement process was extensively consulted upon and resulted in a contract which was aligned with market standards of the time.

- This process resulted in the selection of two reputable counterparties trading as an unincorporated joint venture: Clough Limited, a tier 1 Australian builder,[1] and Elecnor Australia's parent company (Elecnor S.A.), a listed Spanish entity with demonstrated experience in complex transmission infrastructure.
- The EPC contract model was considered by the AER to be a conservative risk allocation that transferred most of the project risk to the contractors. There was no indication that the contract price would be insufficient or that the risk allocation, which reflected market standards of the time, was inappropriate.
- The fixed contract price agreed with SEJV was comparable to the Best and Final Offers (**BAFOs**) submitted by other tenderers.
- The contractor's performance of the EPC contract was also secured by parent company guarantees to support Elecnor Australia and the bonds and performance guarantees provided by Clough Limited. Furthermore, the EPC contract included mechanisms for variation claims and extensions of time, which were appropriate to manage project risks.

In summary, the EPC contract was robust and reflected best practice of the time.

Second, as set out in Attachment 2, having entered into the contract, Transgrid managed the contract appropriately. Transgrid exercised the review and control mechanisms available to it. In accordance with the terms of the EPC contract, Transgrid had limited day-to-day control and was only provided with high level monthly reports until August 2023. Interference or instructions from Transgrid that were inconsistent with the requirements of the EPC contract could have led to Elecnor Australia (the remaining contractor in SEJV following the insolvency of Clough in December 2022), claiming extensions of time and additional costs and increase the difficulty of Transgrid enforcing claims for delay damages (and in fact, such claims were made). Transgrid took steps to enforce the contract and, when challenges arose, took additional steps outside of its strict contractual obligations, including providing additional resources and advance payments to ensure the contract remained on foot.

Third, the Contract Failure occurred not because the terms of EPC contract were insufficient or due to Transgrid's management, but as the result of an accumulation of circumstances beyond Transgrid's reasonable control:

- Transgrid had appropriately managed the risk of cost increases by primarily allocating them to Elecnor Australia under the EPC contract.
- The insolvency of Clough was not caused by PEC, but impacted the ability of Elecnor Australia to deliver PEC under the terms of the EPC contract. Transgrid did not have control over the delay in Clough transferring project records and systems nor did Transgrid have control over the federal labour agreement being transferred to Elecnor Australia. However, the delays associated with the insolvency of Clough affected Elecnor Australia's ability to properly resource the project and accurately forecast the costs of completion, which culminated in substantial programme slippage. Transgrid was only able to understand

[1] A tier 1 contractor is a construction company that can perform most of the required work on a project with its own employees and equipment. Tier 1 contractors usually have a large balance sheet (annual turnover greater than $500 million) and can take on the project risk. Also known as 'general' or 'prime' contractors.

the full extent of the cost overruns once open book access to the cost to complete data was provided to Transgrid in August 2023. By this time, the financial position of the contractor was precarious.

- Transgrid had no control over the extraordinary cost environment in which Elecnor Australia found itself in. While Transgrid assisted Elecnor Australia with cashflow and other measures, Transgrid could not have prevented the contract losses reaching such a magnitude that Elecnor Australia was facing. Elecnor Australia would have been insolvent without additional funding that its parent was not willing to provide, beyond the substantial parent guarantee that had already been provided, without a reset of the delivery arrangements for PEC.
- Transgrid had no control over how Elecnor Australia or its parent company responded to the challenges impacting the construction industry, cost environment or issues experienced by the project, including sub-contractor arrangements.

This event did not occur nor is justified solely on Transgrid's decision making process but was caused by external circumstances outside of Transgrid's reasonable control which became apparent in August to October 2023 and which compelled Transgrid to make a business decision to address and rectify the adverse consequences of the event on PEC or otherwise let the project fail.

2.3 Event was not reasonably foreseeable

The test is whether the Contract Failure (or an event of a similar kind) could not reasonably have been foreseen by the TNSP, at the time of the making of the revenue determination. The assessment of reasonable foreseeability involves the interpretation of two important questions: (i) when reasonable foreseeability is assessed and (ii) what standard of foreseeability is to be applied.

As this is the first transmission reopener application the AER has received, it has not previously had to consider the detail of how the 'not reasonably foreseeable' test is interpreted and applied. Those questions therefore require close consideration by the AER on this application.

In addressing these questions, the AER must adopt the interpretation that:

- will best achieve the purpose or object of the capex reopener function,[2] and
- enables the capex reopener provisions to operate harmoniously with the regulatory scheme for making transmission revenue determinations. The relevant aspects of the regulatory scheme under Chapter 6A are outlined below.

2.4 When reasonable foreseeability is assessed

The purpose of the reasonable foreseeability test is to ensure that TNSPs appropriately forecast their costs as part of their revenue determination process. The reopener should not be available for costs which the TNSP should have foreseen and then addressed through the determination process either by obtaining an appropriate cost allowance, or via a pass-through event or as a contingent project. For the reasons outlined below, Transgrid submits that the date for assessing reasonable foreseeability is 2 December 2022, being

[2] NEL, Schedule 2, Clause 7.

the date Transgrid was required to submit its revised revenue proposal for the 2023-2028 RCP (**Revised Revenue Proposal**).

The 'making' of the revenue determination involves a prescriptive 'propose–respond' regulatory process. The stages of that process include:

- the AER publishing its framework and approach paper
- the TNSP submitting a revenue proposal
- the AER publishing a draft determination
- the TNSP submitting a revised revenue proposal, and
- the AER reaching and publishing its final determination.

Throughout the process, the AER is also required to ensure that affected participants, network service users and user or consumer groups are informed of, and given reasonable opportunity to make submissions about, the material issues under consideration.[3]

The NER contain prescriptive time periods and limitations on TNSPs' revenue proposals and submissions, in order for the AER to have sufficient time to assess the proposals, and to ensure that all stakeholders are given time to comment meaningfully, before the AER makes its determination. The revenue determination is made by the AER having regard to the information set out in clause 6A.12.1(a1): principally, the information contained in or accompanying the TNSP's revenue proposal, and submissions made by stakeholders.

The component of the revenue proposal that is relevant for a capex reopener is the forecast capex for PEC, in this case. Clause 6A.6.7 requires that a TNSP must submit the total forecast capex amount which it "*considers is required in order to"* meet the capex objectives. That is a forecast made at the time when the TNSP submits its initial revenue proposal – typically, more than 12 months before the AER makes its final determination.

If, after its preliminary examination, the AER decides that the TNSP's revenue proposal does not comply with the NER requirements, the TNSP must resubmit its revenue proposal. But clause 6A.11.2(b) provides that the TNSP may only make changes to its revenue proposal to address the matters raised in the AER's decision.

Similarly, the TNSP may submit a revised revenue proposal in response to the AER's draft revenue determination. In this case, Transgrid's deadline for submitting its Revised Revenue Proposal was 2 December 2022. Clause 6A.12.3(b) of the NER provides that, in its revised proposal, the TNSP may only make revisions to its initial proposal *"so as to incorporate the substance of any changes required by, or to address matters raised in, the draft decision*." If the TNSP submits a Revised Revenue Proposal or other submission that goes beyond the permitted scope, or which is submitted after the relevant deadline, those submissions are not required to be taken into account by the AER in making its final revenue determination.

[3] NEL, section 16.

As can be seen from the above, both the extent to which, and the time when, a TNSP may submit additional information regarding its forecast capex for a particular project are tightly limited by the 'propose–respond' procedural framework.

Therefore, when interpreting the clause 6A.7.1(a)(1) 'not reasonably foreseeable' criterion against the 'propose – respond' framework enshrined in Part E of Chapter 6A, Transgrid submits that it would be inappropriate for the AER to apply the reasonable foreseeability test only at the date when the AER makes and publishes its revenue determination. The critical question is whether the reopener event was 'reasonably foreseeable' by the TNSP, and the TNSP's last opportunity to make submissions to the AER on that question will fall several weeks, if not months, before the AER publishes its final determination. In the case of Transgrid's 2023-2028 Revenue Determination, its deadline for submitting its Revised Revenue Proposal fell more than 4½ months before the AER made its revenue determination on 28 April 2023.

Transgrid therefore submits that the appropriate date at which to apply the 'not reasonably foreseeable' test is the date when the TNSP is required to submit its Revised Revenue Proposal, rather than the date on which the AER publishes its revenue determination. For Transgrid's 2023-2028 Revenue Determination, that date was 2 December 2022.

2.5 The standard of foreseeability

The expression "*could not reasonably have been foreseen by the provider*" in clause 6A.7.1(a)(1) must be interpreted in the way that will best achieve the purpose or object of the capex reopener mechanism[4], and so that it operates harmoniously with the mechanism for determining a TNSP's capex allowance through the revenue determination process in Chapter 6A of the NER. In particular, the criteria in clause 6A.7.1(a) must be interpreted and applied in a way that maintains the incentive properties of the *ex-ante* cap, while also limiting TNSPs' exposure to the full risks and costs of uncontrollable shocks that could not have been provided for through the ordinary revenue determination process.

As in any other legal or regulatory setting, the proper meaning of an evaluative criterion such as 'not reasonably foreseeable' requires close attention to the setting in which the test is to be applied, rather than by reference to some universal or abstract meaning.[5] In this setting, it would be a clear error if, for example, the AER were to apply the 'not reasonably foreseeable' criterion by reference to the low threshold of foreseeability that is applied in the very different exercise of a court determining whether one person owes a duty of care in negligence to another to avoid various risks of harm in a particular factual setting.

When a TNSP submits a forecast of its capex for a forthcoming regulatory period, the AER is required to assess whether that forecast reasonably reflects the efficient capex that a prudent TNSP would require, and a 'realistic expectation' of the cost and other inputs that are required to achieve the capex objectives.[6] In the *ex-ante* revenue cap framework, that forward-looking 'realistic expectation' limb has an important role to play in ensuring that a TNSP's revenue allowance is not inflated by over-conservative projections or assumptions

[4] NEL, Schedule 2 clause 7.

[5] As a recent example see *CRS v Secretary, Department of Home Affairs* [2024] FCA 619 at [77] & [131]-[133], applying the 'reasonably foreseeable future' test stated in *NZYQ v Minister for Immigration* [2023] HCA 37.

[6] Clause 6A.6.7.(c)(3).

about the costs and other risks that the TNSP will face over that five-year regulatory period. In making that assessment, the AER is also required to have regard to AEMO's most recent ISP.[7]

That feature of the ex-ante revenue cap framework is important in interpreting the 'not reasonably foreseeable' requirement when the AER is asked to consider a capex reopener during the 5-year regulatory period. In order to align with, and maintain, the incentive properties that are embedded in the clause 6A.6.7 capex criteria, the 'not reasonably foreseeable' test in clause 6A.7.1(a)(1) should be interpreted to align with the 'realistic expectation' limb of the capex criteria.

In substance, the question that the AER is therefore required to ask is: was the capex required to rectify the adverse consequences of the event (or of an event of a similar kind) a cost that a prudent and efficient TNSP would, during the revenue determination process, realistically have expected to incur during the forthcoming 5-year regulatory period? If yes, then no capex reopener ought to be allowed, even if the event satisfies all of the other clause 6A.7.1(a) criteria. If no, and if the event satisfies all of the other criteria – including that it was beyond the TNSP's reasonable control and requires the TNSP to incur unexpected capex exceeding 5% of the value of its RAB – then it is appropriate, and consistent with the *ex-ante* incentive framework for the capex reopener to be allowed.

Conversely, if the AER were to apply different thresholds at the revenue determination and capex reopener stages, then there may be a wide variety of contingencies and risks that would fall between two stools: that is, the AER might have assessed the risk as not representing a 'realistic expectation' of the TNSP's cost input and other assumptions at the revenue determination stage, but might later refuse a capex reopener on the basis that the risk was 'reasonably foreseeable' by the TNSP at the same time – even if the event is otherwise of a magnitude and significance that satisfies all of the other capex reopener criteria.

2.6 Was the event reasonably foreseeable?

When Transgrid submitted its Revised Revenue Proposal on 2 December 2022, the Contract Failure (or an event of a similar kind) could not reasonably have been foreseen by Transgrid. As set out in section 6 of Attachment 2, at that time, the construction of the project had been delayed due to a delay to obtaining Commonwealth environmental approvals, but this would not be an ongoing issue and progress on the project to the end of 2022 proceeded in accordance with the EPC contract. Transgrid was aware of a potential Clough insolvency[8] and was taking active steps to ensure the project would continue to proceed with as little interruption as possible if this occurred. In preparing for a potential Clough insolvency, Transgrid was mindful that under the EPC contract, Elecnor Australia had a right to assume Clough's responsibilities under the contract in the event of a Clough insolvency.

Following the Clough insolvency in December 2022, Elecnor Australia remained engaged in the project and re-committed to delivering the project under the EPC contract, notwithstanding the loss of Clough as a JV partner. The EPC contract was a fixed price contract which transferred the majority of the project risk to the contractor. The project delays resulting from the severe weather conditions were not unusual in the context of a large, complex infrastructure project, had resolved by February 2023 and it was reasonable to assume

[7] Clause 6A.6.7(e)(11).

[8] Clough was placed into voluntary administration on 5 December 2022.

that delays could be managed by the delay liquidated damages regime. The alleged cost escalations were of a magnitude that was significantly lower than the Performance Securities (see Attachment 2 for these figures), therefore, Transgrid believed the cost overruns could be managed by the Performance Securities.

As at 28 April 2023, Transgrid believed that Elecnor Australia's parent company had sufficient incentive to remain committed to the project and at this point Transgrid did not have any information to suggest that Elecnor Australia's parent company would not be able to stand behind the Performance Security.

For the reasons outlined above, the Contract Failure was not reasonably foreseeable by Transgrid as at 2 December 2022, or even as at 28 April 2023, if the AER considers that is the appropriate date at which the 'not reasonably foreseeable' test should be applied.

3. Forecast expenditure not accepted or substituted in relation to the event

Clause 6A.7.1(a)(2) requires that no forecast capex was accepted or substituted by the AER for the 2023-2028 RCP in relation to the event.

Transgrid's original capex forecast included expenditure related to the EPC contract. It did not include forecast capex for the Contract Failure. The rectification costs claimed are not costs that were included, or contemplated, in the capital allowance provided by the AER.

4. Capex proposed to rectify the event

Clause 6A.7.1(a)(3) requires that the TNSP proposes to undertake capex to rectify the adverse consequences of the event.

Executing an ICC contract with Elecnor Australia was the option selected to rectify the adverse consequences of the event. This option has a net forecast cost to complete PEC of $3,628 million. Further detail on the options analysis undertaken by Transgrid in order to select the option to recontract with Elecnor Australia can be found in Attachment 3.

A detailed explanation of the reopener amount of $1,142 million is provided in Attachment 7, which explains that it is the additional costs to be incurred by Transgrid to rectify the adverse consequences of the event.

5. Capex amount satisfies the threshold requirements

Clause 6A.7.1(a)(4) requires that the total of the capex required during the 2023-2028 RCP to rectify the adverse consequences of the event:

- exceeds 5% of the value of the regulatory asset base for the TNSP for the first year of the relevant RCP, and
- is such that, if undertaken, it is reasonably likely (in the absence of any other reduction in capex) to result in the total actual capex for that RCP exceeding the total of the forecast capex for that RCP as accepted or substituted by the AER.

The value of Transgrid's opening regulatory asset base for 2023-24 is $9,147 million, and 5% of this amount is $457 million. As noted in section 4, the capex required to rectify the adverse consequences of the event is $1,142 million, which substantially exceeds the threshold.

Table 1 below compares Transgrid's current capex forecasts against its regulatory allowances for the 2023-2028 regulatory control period, split between BAU capex,[9] contingent projects (HumeLink and VNI West) and PEC. Transgrid's forecast for PEC over this period is $2,616 million, which is an increase of $1,511 million compared to the AER's PEC allowance of $1,104 million.[10] This increase is the key contributor to Transgrid exceeding its total 2023-2028 net capex allowance by $1,539 million as shown in Table 1 below, which satisfies the requirements specified in clause 6A.7.1(a)(4).

[9] Defined as being non-PEC capex included within the AER's 2023-2028 Revenue Determination for Transgrid.

[10] The cost information presented in relation to clauses 6A.7.1(a)(4)(ii)) and 6A.7.1(a)(5) differ from some of the values presented in the main application. These provisions focus on the 2023-2028 regulatory control period and therefore do not consider costs prior to 2023-24. Additionally, this cost information relates to total capex values, whereas the main application is focused on incremental capex that is the direct result of the event.

Table 1: Transgrid's forecast capex and overspend amounts ($m, 2022/23)

		2023-24	2024-25	2025-26	2026-27	2027-28	Total
Capex forecast	BAU capex	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	PEC capex	717	940	746	213	-	2,616
	HumeLink stage 1 part 1	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	HumeLink stage 1 part 2	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	VNI West stage 1 (CPA1)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	HumeLink stage 2	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Total	**1,221**	**2,098**	**3,117**	**1,904**	**855**	**9,196**
Capex allowance	BAU capex	280	301	250	249	279	1,359
	PEC capex	879	225	-	-	-	1,104
	HumeLink stage 1 part 1	90	-	-	-	-	90
	HumeLink stage 1 part 2	102	126	-	-	-	228
	VNI West stage 1 (CPA1)	476	370	64	-	-	911
	HumeLink stage 2	43	1,796	1,811	315	-	3,965
	Total	**1,870**	**2,818**	**2,125**	**564**	**279**	**7,656**
Disposals	Disposal forecast	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Disposal allowance	5	5	5	5	5	27
Net capex overspend		**(645)**	**(716)**	**989**	**1,337**	**574**	**1,539**

Notes: The forecast capital expenditure reflects our current best estimates. For HumeLink and VNI West Stage 1 (CPA1), the forecast project costs are very closely aligned with the AER's allowance although there are timing differences. For HumeLink, there is a minor underspend in the previous regulatory period which offsets the overspend shown in the 2023-28 regulatory period. For VNI West, the timing of capital expenditure has been revised to best align with project timelines within the latest ISP. This has ultimately resulted in LLE and contractor costs being incurred later in the regulatory period.

6. Reliability and security implications of potential capex reductions

Clause 6A.7.1(a)(5) requires Transgrid to demonstrate that it is not able to reduce capex in other areas to avoid the total actual capex for the RCP exceeding the total forecast capex for the RCP (being the consequence referred to in clause 6A.7.1(a)(4)(ii)) without materially adversely affecting the reliability and security of the relevant transmission system.

This pre-condition requires Transgrid to consider whether capex could be reduced to eliminate the overspend described in Table 1, without impacting reliability or security of supply. Importantly, the pre-condition does not require Transgrid to make any such reduction, and Transgrid does not propose to amend its capex plans, noting that these plans satisfy the capex objectives in the NER.

To address this pre-condition, Table 2 shows Transgrid's total BAU capex allocated between capex focused on:

- achieving improved security and reliability outcomes, and
- realising net economic benefits.

The table excludes the capex allowance for contingent projects as these projects are fully committed and critical to AEMO's Optimal Development Path in its ISP. As the total forecast for capex focused on realising net economic benefits is only [redacted] million over the 2023-2028 regulatory period, it would not be possible to achieve the required reduction of $1,539 million without impacting safety, security and reliability capex. Accordingly, the pre-condition in clause 6A.7.1(a)(5) has been satisfied.

For the avoidance of doubt, Transgrid is not proposing any reduction to its capex plans, which are as set out in Table 2 below, noting that the vast majority of Transgrid's capex is focused on security and reliability. It is also important to note that these forecasts are point in time estimates and subject to change as Transgrid progresses through the 2023-2028 RCP.

Table 2: Transgrid's current BAU capex forecasts for the 2023-2028 regulatory period, excluding contingent projects

			2023-24	2024-25	2025-26	2026-27	2027-28	Total
Current forecast	Security and reliability	Repex	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Augex	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		ICT	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Fleet & property	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Total	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	Economic benefits	Repex	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Augex	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		ICT	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Fleet & property	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
		Total	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Disposal forecast			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Disposal allowance			**5**	**5**	**5**	**5**	**5**	**27**
Total current forecast			[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Original allowance			**280**	**301**	**250**	**249**	**279**	**1,359**
Net overspend			**(44)**	**(45)**	**53**	**47**	**(10)**	**-**

7. Reliability and security implications of failure to rectify event

Clause 6A.7.1(a)(6) requires Transgrid to demonstrate that a failure to rectify the adverse consequences of the Contract Failure would be likely to materially adversely affect the reliability and security of the relevant transmission system.

7.1 How to apply the precondition

For the purpose of applying this precondition, Transgrid considers that the following approach is required.

- The adverse effect on reliability and security should be assessed on a forward-looking basis by having regard to the impact of failing to rectify the event on the transmission system as required to be built to meet the NEM reliability standard and to ensure operation of the system within the required technical limits. The clause does not require an imminent issue on the network that exists at the time of the event. The reopener relates to capex, which involves the construction of long-life assets and need to satisfy the long-term reliability standards and must implicitly include an assessment of the need which that capex is addressing and the future state of the transmission system without the rectification.[11]
- The precondition requires an assessment of the reliability and security impacts in the factual case where the event is remedied and the counterfactual case where the event is not. In this case, the consequences of the Contract Failure, if unremedied, is that PEC is not delivered and the rectification which maximises consumer benefits is a new contract where it is delivered. For the purposes of applying this precondition, Transgrid is taking a conservative approach by assessing the reliability of the network with Separable Portion 1 (**SP1**) completed (as it was substantially completed when the event occurred), even though rectification costs would need to be incurred to achieve that outcome. This approach sets a higher hurdle by only examining the impact of not completing Separable Portion 2 (**SP2**) on the reliability and security of the transmission system, rather than also including the absence of SP1.
- As PEC is an interconnector between New South Wales and South Australia, the impacts in both those regions need to be considered. The 'relevant transmission system' is the transmission systems of South Australia and New South Wales, as this condition is concerned with where the adverse consequences of the event fall. PEC is a cross-border interconnector allowing electricity to flow between jurisdictions. PEC emerged as the preferred option identified in ElectraNet's 'South Australia Energy Transformation' RIT-T, which was aimed at reducing the cost of providing secure and reliable electricity to South Australia and enhancing system security in South Australia, therefore, the transmission systems of New South Wales and South Australia are relevant. PEC (at the time called Riverlink) was identified in the 2018 ISP; AEMO described that an interconnector between South Australia and New South Wales was "*vital for system security.*"

[11] This is also consistent with transmission planning which uses a 10 to 20-year planning horizon and the capex objectives and capex criteria in clause 6A.6.7 of the NER which are predicated on providing a capital allowance to allow the TNSP to meet quality, reliability and security of transmission services over the RCP.

7.2 Reliability and security impacts

The importance of PEC to ensuring a reliable and secure transmission network is demonstrated by AEMO's inclusion of PEC as an actionable ISP project in the ISP, having originally emerged from Transgrid's joint planning obligations with ElectraNet and AEMO under clauses 5.14.3(a) and 5.14.4 of NER. The purpose of the ISP is to "*establish a whole of system plan for the efficient development of the power system that achieves power system needs for a planning horizon of at least 20 years for the long term interests of the consumers of electricity.*"[12] 'Power system needs' are defined in the NER and include the reliability standard and power system security, as those terms are defined under the NER.[13] In preparing the 2024 ISP AEMO considered two power system needs being:

- reliability, specifically resource adequacy and capability, and
- security, specifically frequency and inertia, voltage management and system strength and system restoration and flexibility.[14]

GHD have been engaged to provide an expert report through a review of public domain information to compile a statement of facts that documents the reliability and security benefits that are expected to be delivered by PEC when fully operational. The statement of facts considered various sources of information. The information gathered has been used to assess the extent of the reliability and security benefits that PEC is expected to deliver and consider whether failing to complete PEC stage 2 would materially adversely affect reliability and security of the NEM. The review supports reliability and security impacts on South Australia, New South Wales and Victoria attributable to the completion of PEC stage 2. GHD's report is provided as Appendix 6a.

The specification of PEC as an actionable ISP project is demonstrated by the impacts of a failure to complete SP2 (constituting the failure to rectify the event) which would materially and adversely affect the reliability and security of the transmission networks of South Australia and New South Wales. These impacts include:

- **Compromised ESOO Reliability**: The failure to complete PEC SP2 would result in ESOO reliability being further compromised. This shortfall would require additional network services - services from NSPs that are essential to the safe, secure, and efficient operation of the transmission network, such as deploying extra synchronous condensers to improve reliability. These have high risk of uncertainty of delivery timeframes.
- **South Australia Reliability Gap**: In 2026, South Australia's transmission network will fall below AEMO's reliability standard. This is currently expected to be rectified by the finalisation of PEC SP2. If SP2 is not built, South Australia's transmission network reliability will be materially impacted because expected unserved energy will remain above the interim reliability measure (**IRM**), with the unserved energy gap growing wider from 2030 with further gas turbine retirements.
- **Reduced New South Wales Transfer Capacity**: PEC SP2 will provide essential transfer capacity between South-West New South Wales and future transmission projects such as HumeLink. Without

[12] Clause 5.22.2 of the NER.
[13] Clause 5.22.3(a) of the NER.
[14] AEMO, ISP 2024, p 38.

SP2, the ability of the New South Wales system to maintain reliability by leveraging additional supply from neighbouring regions would be compromised.

- **Compromised System Security**: SP2 will elevate fault levels in SWNSW, thereby strengthening the grid's capacity to meet minimum fault level requirements and enhancing overall system security; without rectification, other sources of system security will need to be sought.

The failure to complete SP2 would have a material impact on an already challenged level of reliability in South Australia. In 2026-27, all units of Torrens Island B and Osborne Power Station are scheduled to retire. As a result, in 2026, South Australia will violate the IRM constituting an increase in reliability risks for the state. In 2027-28, SP2 would reduce reliability risks below the IRM to negligible levels for the remainder of the reliability forecast. Furthermore, various gas and liquid fuel generators in South Australia have advised retirement in 2030 and 2032, reducing project supply availability and slightly increasing reliability risks in South Australia. SP2 therefore provides firming capacity for renewables in South Australia. Without SP2, South Australia has no immediate pathway to return below the required reliability standard and unserved energy will increase, further increasing reliability risks in South Australia from 2030. This constitutes a material adverse impact on reliability.

While the impacts on South Australia are substantial, even if the reliability and security impacts on the New South Wales transmission system are considered in isolation, the reduction in New South Wales transfer capacity and compromised system security referred to above, are sufficiently material to meet the precondition.

8. Exclusions for pass through event or contingent projects

Clause 6A.7.1(a)(7) requires that the event is not a 'pass-through event' or a 'contingent project.'

The event is not a cost pass through event under clause 6A.7.3 of the NER for Transgrid's 2023-2028 Revenue Determination.

The event is not a contingent project (as defined in clause 6A.8.1A) in relation to the 2023-2028 Revenue Determination under clause 6A.7.1. The event is the failure of the EPC contract and not PEC itself. In any event, while PEC was a contingent project for the 2018-2023 Revenue Determination, PEC was not a contingent project in the 2023-2028 Revenue Determination about which this Application is made.

9. Timing of application

Clause 6A.7.1(b) of the NER states that an application referred to in clause 6A.7.1(a) must not be made within 90 business days prior to the end of the regulatory year, which is 30 June.

This application is made on 13 February 2026 which is not within 90 business days prior to the end of the regulatory year.

10. Regulatory compliance checklist

Table 3 below sets out a checklist which demonstrates the compliance of this Application with the NER requirements. It references where the relevant information can be found in this Attachment.

Table 3: Transgrid's compliance with the NER provisions

Clause	Detail	Reference
6A.7.1(a)(1)	An event that is beyond the reasonable control of the TNSP has occurred during that regulatory control period and the occurrence of that event during that period (or of an event of a similar kind) could not reasonably have been foreseen by the provider at the time of the making of the revenue determination ('the event'). … In this paragraph (a), a reference to an event includes a series of events or a state of affairs, which may include a greater than anticipated increase in demand.	Section 2 of this Attachment
6A.7.1(a)(2)	No forecast capital expenditure was accepted or substituted by the AER for that period under clause 6A.6.7(c) or clause 6A.13.2(b)(4) and (5) (as the case may be) in relation to the event that has occurred.	Section 3 of this Attachment
6A.7.1(a)(3)	The TNSP proposes to undertake capital expenditure to rectify the adverse consequences of the event.	Section 4 of this Attachment
6A.7.1(a)(4)	The total of the capital expenditure required during the regulatory control period to rectify the adverse consequences of the event: (i) exceeds 5% of the value of the regulatory asset base for the relevant TNSP for the first year of the relevant regulatory control period, and (ii) is such that, if undertaken, it is reasonably likely (in the absence of any other reduction in capital expenditure) to result in the total actual capital expenditure for that regulatory control period exceeding the total of the forecast capital expenditure for that regulatory control period as accepted or substituted by the AER in accordance with clause 6A.6.7(c) or clauses 6A.13.2(b)(4) and (5) (as the case may be).	Section 5 of this Attachment
6A.7.1(a)(5)	The TNSP can demonstrate that it is not able to reduce capital expenditure in other areas to avoid the consequence referred to in clause 6A.7.1(a)(4)(ii) without materially adversely affecting the reliability and security of the relevant transmission system.	Section 6 of this Attachment
6A.7.1(a)(6)	A failure to rectify the adverse consequences of the event would be likely to materially adversely affect the reliability and security of the relevant transmission system.	Section 7 of this Attachment and Appendices 6a and 6b.
6A.7.1(a)(7)	The event is not a pass-through event or a contingent project.	Section 8 of this Attachment
6A.7.1(b)	An application referred to in paragraph (a) must not be made within 90 business days prior to the end of a regulatory year.	Section 9 of this Attachment

11. Appendices

The following appendices are provided to support compliance with clause 6A.7.1(a)(6):

- Appendix 6a: Statement of facts: Reliability and security impacts, GHD, and
- Appendix 6b: Letter of support, ElectraNet.